The Change to the Pension Fund Assumed Rate of Return

There has been a lot of buzz lately about the change the Pension Board made to the Pension Fund's "assumed rate of return" or "rate of return assumption". We hope this article provides answers to some of the questions around the change. If you're concerned about the funding of the Pension Fund, employee contributions, or BackDROP, please read the entire article and contact Retirement Plan Services (RPS) if you have additional questions.

Definitions

Actuarial assumptions are used to estimate the present value of benefits to be paid in the future for all current members of the Employees' Retirement System. This means that we estimate the amount of money the Pension Fund needs to pay out all future benefits, assumptions have to be made.

There are two major types of assumptions:
Demographic assumptions are assumptions about the benefits that are paid out including normal, early, and disability retirements, death and survivor benefits, and contribution withdrawals.
Economic assumptions are assumptions about the money in the Pension Fund such as the assumed rate of return of investments (how much money the fund makes from its investments), inflation, salary increases, and payroll growth.

Change

When the Pension Fund is valued, the new assumed rate of return will be used. Changing this assumption may also affect employee contributions and the calculation of BackDROP benefits. This change does not affect the multiplier used to calculate pension benefits.

2017	2018-2019	2020 & beyond
8%	7.75%	7.5%

Rationale

After carefully reviewing investment returns of the Pension Fund over the last several years along with future projections, the data showed that over the next 10 years, the current assumption of achieving an 8% rate of return was projected to be achieved under 40% of the time. This means that currently the Pension Fund is assumed to earn 8% return on its investments when the data shows there's only a 40% chance that 8% return could be reached. The Pension Board determined that a rate of 7.5% would be achievable over the next 10 years and the change should come in steps as outlined in the table above.

What's Affected

Plan Funding
The rate of return assumption is important because the amount of money generated by investments is one of the factors used to determine how well funded a pension plan is. If an unachievable rate of return is used, the value of the fund is inflated, and there could be less money to pay benefits than the plan administrators believed was available. For example, if you invested money and assumed you'd get an 8% return, but only make 7.5% return, you have less money now than you thought you would have had.

BackDROP
The rate of return assumption is also the interest rate applied to the BackDROP lump sum. A member retiring with a BackDROP in 2018 will receive the lump sum (number of months in BackDROP period multiplied by the monthly benefit amount) plus 7.75% interest. The interest rate in effect at retirement is applied to the entire lump sum amount.

RPS strives to provide information valuable to members making the decision of when to retire. If you are BackDROP eligible and are interested in exploring the impact the change may have on your benefit payment, please contact RPS at 414-278-4207. The update to the retirement calculator necessary to incorporate the change is in progress. However, we anticipate that it will take three months to complete the update. RPS is also available to answer any questions you may have regarding your retirement benefits and the change in the assumed rate of return.